



The Institute of Chartered Accountants of India
Western India Regional Council

Intensive Workshop on Companies Act, 2013

[from SME Perspective]

Date: 4th July, 2014

Venue: Seminar Room [Mayor Hall], C D Barfiwala Marg,
Andheri (West), Mumbai - 400 058.

Topics

- Related Party Transactions
- Corporate Governance
- Acceptance of Loans and Deposits
- Guarantees
- Lending and Investments
- Frauds and Management Responsibility

Faculty

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Jointly with Andheri West CPE study circle

The Companies Act, 2013

Some Understanding and some confusions
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04-07-2014

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The Companies Act, 2013

• Topics for discussion:

- Frauds and Management Responsibility
- Accepting of deposits & Loans (borrowings)
- Giving of Loans, Guarantees, securities
- Making Investments
- Related Party Transactions

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Cultural Changes

- Changes in provisions are not only in letter but compliance in spirit of law is desired.
- More responsibility is cast on Professionals, KMPs of the company.
- Penalties have gone up multifold

Frauds & Management Responsibility - Key Drivers

- Sec 2(6) – Associate Company – One co. Having Significant Influence on the another – Co. Which holds at least 20% of the paid up capital or control of business decisions under an agreement. (Subsidiary Co. Not included)
- Sec 2 (51) - 'Key Managerial Personnel' – includes CEO, MD CFO, WTD, CS and such other officer as may be prescribed – co is expected to identify and designate in adopting policy for KMPs

Frauds & Management Responsibility - Key Drivers

- Sec 2(60) – ‘Officer in default’ - KMP and Board of Directors. Further any job or responsibility delegated by either KMP or Board, such authorized person will be an officer in default
- **All Cos. needs to have policy on KMPs.** - though u/s 203 - cos. Having paid up cap of 10 cr or more are required to appointment KMPs
- Sec 2 (76) – Related Party – wider coverage – now also includes – ‘any body corporate who is accustomed to act’ , KMPs, Holding –subsidiary – Associate Co. (**Co needs to pay attention**)

Frauds & Management Responsibility - Key Drivers

- Steps to be taken by the management to detect frauds in time –
 - Risk Management Policy – disclosure u/s 134 – entry of Air Asia – its impact on Go Air, Jet.
 - Same thing happened when DOCOMO entered telecom market.
 - Entry of Reliance Media Entertainment wiped out many players from the market – latest being ‘Network 18’

Frauds & Management Responsibility - Key Drivers

- Appointment of Internal Auditor – u/s 138 – though applicable to cos. Having turnover > 200 cr OR borrowings > 100 cr – others need to have Internal Audit function in place.
- Impact of pending litigations in financial statements – u/s 134.
- Provision for material foreseeable losses – like derivative contracts.

Frauds & Management Responsibility - Key Drivers

- Constitution of Vigil Mechanism – u/s 177(9)
- It is similar to Whistle Blower Mechanism
- Difference is - policy must provide for direct access to Chairman of Audit Committee OR director responsible for such function
- **Satyam in case** – how other employees could not find it out when their salaries were delayed

Frauds & Management Responsibility - Key Drivers

- Sec 447 - Fraud means – in relation to the affairs of the company or any body corporate, includes any act, omission, concealment of any fact or abuse of position committed by any person..... with intent to deceive, to gain undue advantage from, or to injure the interest of the company, its shareholders, creditors
.....
- It is much wider than Contract Act provision

Frauds & Management Responsibility - Key Drivers

- Sec 448 – False Statement – if in any return, report certificate, financial statement, prospectus – makes a statement which is false in any material particulars, knowing it to be false OR omits any material facts, knowing it to be material.
- Show me how you will escape?
- Only options is to be diligent, prudent and update.
- Of late RBI has come out with circular making training of management of Co-operative banks and Co-operative Credit Societies mandatory.

Frauds & Management Responsibility - Key Drivers

- Sec 449 – Punishment for False evidence – upon any examination on oath or affidavit –
- Can Dhoni be booked by India Cement for suppression of material facts

Acceptance of Deposits

- Sec 73 – applicable to all the companies for accepting deposits even from Members. (proposed – Pvt. Cos. Can accept from Members upto 25% paid-up cap & free reserves OR 100% of free reserves)
- Sec 76 – applicable to certain eligible public co. – net worth not less than 100 cr OR turnover not less than 500 cr.
- It means, as in C A 1956, pvt co could have accepted deposits from its members, now unless it comply with Sec73, it can not. (some relaxation is expected)

Acceptance of Deposits....

- Now, not any public co can accept deposits unless it is eligible u/s 76.
- Rule 2(c) of The Companies (Acceptance of Deposits) Rules, 2014 – ‘Deposits’ mean –
- ‘any receipt of money by way of deposit or loan or in any other form.’

Acceptance of Deposits....

- Some exclusions from def. Of Deposits, which warrant attention –
- Any amount received by issuing CPs or any other instruments as per RBI guidelines.
- Share application money/advance against allotment of securities – if security is not allotted in sixty days of receipt and thereafter not refunded in 15 days, then it is treated as deposit.

Acceptance of Deposits....

- ICDs – (keep in mind sec 185)
- Amounts received from directors (Keep in mind sec 188 – Related Party tran.)
- Bonds or debentures compulsorily convertible within 5 years.
- Amounts rece from employees not exceeding annual salary.
- Advance against long term projects for supply of capital goods.

Acceptance of Deposits....

- Formalities –
 - DPT 1 – circular by Regd. AD, Speed Post, Electronic mode.
 - Upload copy on the website – what is official website?
 - Publish in 2 news papers.
 - Issue of deposit receipt.
 - File a copy with ROC – 30 days thereafter advertisement in newspapers.

Acceptance of Deposits....

- Rule 5 - deposit insurance – ‘amount specified in deposit insurance contract shall be deemed to be the amount – in respect of principal + interest due.
- In case of default in repayment insurance co liability is limited upto the amount specified in the contract.
- If the co is not issuing secured deposits, who will safeguard the interest of depositors?

Loans, Guarantees, Investments

- Sec 186 – not exceeding 60% of paid-up capital + free reserves + share premium account OR 100% of free reserves + share premium account
- Unanimous Board Resolution
- Can not be circular resolution.
- Exceeding the limits – shareholders’ approval – special resolution + financial institutions’ approval if the loan is outstanding

Loans, Guarantees, Investments....

- Loans given should be at a rate lower than Govt Securities rate for similar tenor. (new)
- Co. To make separate disclosure in the Financial statement about loans, guarantees given, investments made and purpose for which the recipient will put to use such facility. (new)
- Sec 186 (11) – nothing in this sec apply to loan made, guarantee given or security provided ----- to a co. engaged in the business of providing infrastructural facilities – (activities specified in schedule VI)

Loans, Guarantees, Investments....

- It should have 'by co. who are the business of providing loans, guarantees----- to cos. whose principal business is providing finance to infra. (like IDFC).
- Investment thru' not more than two layers of investment cos. - but it doesn't stop from co. acquiring any co outside India having more than two layers of investment cos. (Voda case)
- Any subsidiary – having any investment sub to meet with the requirement of laws. (banking/mutual fund business.)

Loans, Guarantees, Investments....

- Loans, Guarantees given, security provided to its wholly owned co., joint venture co. Acquisition of shares of wholly owned co. – **Special Resolution not necessary.**
- **Register under this section can be maintained in electronic mode also.**
- **For companies who have followed C A 1956 – special resolution can be passed within one year of its notification.**

Loan to Director, etc.....

- Sec 185 – No co. Shall directly or indirectly, advance any loan, including any loan represented by a book debt to any of its directors or any other person in whom the director is interested....
- For this purpose the expression ‘to any other person in whom director is interested means –
- **Any director of the holding co or of a co. Which is its holding co.....**

Loans to Director, etc.....

- Areas of concern –
 - 'accustomed to act in accordance with --- it becomes a matter of investigation and not merely restricted to what management says. Words covered are BOD, MD or Manager – what about WTD?
 - it talks about only – 'directions or instructions of Board, any director – what about CEO/CFO giving instructions?
 - Whether written instructions or even oral instructions to be looked into?

Related Party Transactions

- Sections 297 & 314 of C A 1956 are now clubbed in Section 188.
- 'Arm's length transaction' – means transaction between two related parties that is conducted as if they were unrelated so that there is no conflict of interest.
- Sec 2(76) – some new dimensions –
 - Clause (ii) - KMP or his relative is covered.
 - Clause (vi) A pub co. In which director or manager is a director OR

Related Party Transaction....

- Holds along with his relatives, more than 2% of its paid-up capital. (earlier transactions between 2 public companies were exempted from Sec297.)
- Any body corporate whose BOD, MD or Manager is accustomed to act in accordance with then advice, directions or instructions of a director or Manager.
- What is 'accustomed to act' – whether only directions/instructions on policy matters or even administrative directions/instructions are covered?

Related Party Transaction....

- If directions/instructions given to WTD attract the provisions of this section?
- So as to arrive at 'accustomed to act' relationship we need some documentary evidence or Oral/circumstantial directions/instructions are enough.
- Clause (vii) – 'any person on whose advice, directions or instructions a director or Manager is accustomed to act (advice given in Professional capacity not covered)
- Whether advice by Mr. Murthy as Mentor – Simlicitor will attract prov. Of this sub clause?

Related Party Transaction....

- Earlier immovable property transactions were not covered in Sec 297 – now this exemption is gone.
- Procedural aspects which needs attention –
 - To be considered at a BM – (Circular Resolution not allowed).
 - At first BM after 01.04.2014 – MBP 1 disclosure to be taken on record.
 - Separate Agenda point and not in any other business.
 - Director shall not be present at the time of discussions in the BM.(whether his presence in the meeting can be considered as in a position of exerting 'Undue Influence'

Related Party Transaction....

- In the following cases - Special Resolution in Members meeting & Member can not vote on such business.
 - Sale, purchase and supply of goods/material > 25% of annual turnover.
 - Sale, buy or dispose off property of any kind (movable /immovable/intangible) > exceeding 10% of Net Worth
 - Leasing of property > 10% of Net Worth OR 10% of turnover.
 - Availing or rendering of services > 10% of Net Worth

Related Party Transaction....

- Appointment to any office or place of profit in the company, **its subsidiary, associate co.** At a monthly remuneration > INR 2.5 lacs.
- Transaction between Holding Co. And Wholly owned subsidiary – **resolution passed by Holding co. Is sufficient.**
- Explanatory statement u/s 101 giving details of transactions and relationship of interested person.
- Section 189 & Rule 16 – Register of such contracts to be maintained. **Entries to be made immediately/asap and in chronological order.**

Related Party Transaction....

- Entries in Register need not be made in the following cases –
 - Where a contract with any body corporate in which director himself together with any other director hold 2% of the paid up cap or less in that body corporate.
 - Where sale, purchase or supply of any goods, materials or services if the value or the cost does not exceed INR 5 lacs in aggregate in any year.
 - The Register shall be in the form MBP₄ and to be preserved permanently.

EXEMPTIONS PROPOSED FOR PVT. Cos.

- Sec 43 – types of Capital – **may not apply**
- Sec 47 – voting Rights – **may not apply**
- Sec 62(1)(a) – Requirement offering shares to the existing shareholders – **may not apply**
- Sec 62(1)(b) – **instead of Special Reso, now Ordinary Reso is ok.**
- Sec 62(2) – **minor change – notice period requirement reduced.**
- Sec 73(2) – Acceptance of deposits from Members – if no is less than 50 – up to 25% of -----**may not apply**

EXEMPTIONS PROPOSED FOR PVT. Cos.

- Sec 101 to 107 & 109 – pertaining to General Meetings – Notice, explanatory statement, Chairman, proxies, demand for poll – shall apply unless..... **Articles provide otherwise – How Articles can provide otherwise, it will become ultra virus, may be betterment provisions can prevail in AOA like more no of days notice**
- Sec 141(3)(g) – appointment Auditors – **limitation of 20 co. – may not apply – pvt. Co may not be counted.**
- Sec 160, 162 – Notice of appointment of directorship, voting individually – **may not apply**

EXEMPTIONS PROPOSED FOR PVT. Cos.

- Sec180 – (Sec293 of 1956) – Restrictions on Powers of the Board – **may not apply**
- Sec185 – loans to directors – which have borrowings not more than twice of paid up cap OR 50 cr which ever is less. –& in whose share capital no other body corporate has invested money – **may not apply**
- Sec 188 – Related parties transactions – **may not apply** – may lead to controversy – as under 1956 transactions between 2 public co were exempted.
- Sec 196 (4) &(5) – requirement of shareholders approval – **may not apply**
- Sec 203(3) – not to appoint KMP in more than one co. – **may not apply**

INFRASTRUCTURE COMPANIES

- To finance Infra projects, co. may issue Preference Shares for a period for more than 20 years (Sec 56) – subject to redemption of such % of shares as may be prescribed on annual basis at the option of Preference Shareholders.
- Except Sec 186 (1) – (loans & investments by the company), rest of the provisions are not applicable to a company engaged in the business of financing of companies **or of (which)** providing infrastructural facilities.
- discuss e.g. Of IDFC.

INFRASTRUCTURE COMPANIES

- Schedule VI – Some e.g. Of Infra projects which are approved – some e.g.
 - Transportation including roads, rails, ports, aviation, **logistic services.**
 - Agriculture – including storage, construction of agro processing units.
 - Water Management – including irrigation, water treatment.
 - Telecommunication
 - Industrial Parks, SEZs.
 - Power including generation, distribution, transmission.
 - **Disaster management services**
 - **Preservation of Monuments & icons**

Keep in touch

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THANK YOU